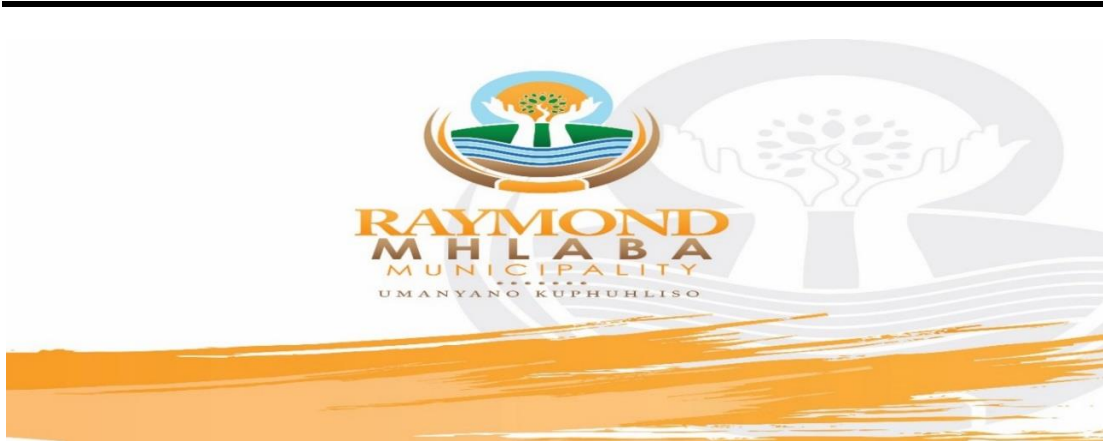




*DRAFT BUDGET 2017/2018*



# **RAYMOND MHLABA EC129**

## **2017/18 TO 2019/20 MEDIUM TERM REVENUE AND EXPENDITURE FORECASTS**

*Prepared in terms of the Local Government: Municipal Finance Management Act (56/2003): Municipal Budget and Reporting Regulations, Government Gazette 32141, 17 April 2009.*



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### **2. GLOSSARY**

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**Adjustments Budget** – prescribed in section 28 of the MFMA. The formal means by which a municipality may revise its annual budget during the year.

**Allocations** – Money received from Provincial or National Government or other municipalities.

**Budget** – the financial plan of the municipality.

**Budget related policy** – policy of a municipality affecting or affected by the budget, such as the tariffs policy, rates policy and credit control and debt collection policy, etc.

**Capital Expenditure** – Spending on assets such as land, buildings and machinery. Any capital expenditure must be reflected as an asset on the municipality's balance sheet.

**Cash flow statement** – a statement showing when actual cash will be received and spent by the municipality. Cash payments do not always coincide with budgeted expenditure timings. For example, when an invoice is received by the municipality it scores as expenditure in the month it is received, even though it may not be paid in the same period.

**DORA** – Division of Revenue Act. Annual legislation that shows the amount of allocations from National to Local government.

**Equitable share** – a general grant paid to municipalities. It is predominantly targeted to help with free basic services.

**Fruitless and wasteful expenditure** – expenditure that was made in vain and would have been avoided had reasonable care been exercised.

**GFS** – Government Finance Statistics. An internationally recognised classification system that facilitates like for like comparison between municipalities.

**GAAP** – General Accepted Accounting Principles. World Wide Accepted Standards.

**GRAP** – Generally Recognised Accounting Practice. The new standard for municipal accounting.

**IDP** – Integrated Development Plan. The main strategic planning document of the municipality.

**KPI's** – Key Performance Indicators. Measures of service output and / or outcome.

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## *DRAFT BUDGET 2017/2018*

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**MFMA** – The Municipal Finance Management Act – no 53 of 2003.  
The principle piece of legislation relating to municipal financial management.

**MTREF** – Medium Term Revenue and Expenditure Framework. A medium term financial plan, usually 3 years, based on a fixed first year and indicative further two years' budget allocations. Also includes details of the previous and current year's financial position.

**Operating expenditure** – spending on the day to day expenses of the municipality such as salaries and wages.

**Rates** – Local government taxation based on an assessed valued of a property. To determine the rates payable, the assessed rateable value is multiplied by the rate in the rand.

**SDBIP** – Service Delivery and Budget Implementation Plan. A detailed plan comprising quarterly performance targets and monthly budget estimates.

**Strategic Objectives** – the main priorities of the municipality as set out in the IDP. Budgeted spending must contribute towards the achievement of the strategic objectives.

**Unauthorised expenditure** – generally, spending without, or in excess of, and approved budget.

**Virement** – a transfer of budget

**Virement Policy** – The policy that sets out the rules for budget transfers. Virements are normally allowed within a vote. Transfers between votes must be taken and approve by Council.

**Vote** – one of the main segments into which a budget is divided, usually at directorate / department level.

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### **3. MAYORAL BUDGET SPEECH**

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### **4. BUDGET RELATED RESOLUTIONS**

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On 29 March 2017 the Council of Raymond Mhlaba Local Municipality will meet in the Council Chamber to consider the Draft IDP and Annual budget of the municipality for the financial year 2017/18. The Council to approved the following resolutions:

1. The council to adopt the Draft IDP for 2017/2018 financial year as a strategic document to guide developmental initiatives and programmes for duration of the period enunciated therein,
    - 1.1.1. The organizational structure for 2017/2018 financial year, which is an annexure to the IDP.
    - 1.1.2. The IDP and Budget 2017/2018 should be made public in terms of section 21A and 21B of the Municipal Systems Act.
    - 1.1.3. The copy of the IDP and Budget 2017/2018 be submitted to the MEC for Local Government in terms of section 32 of the Municipal Systems Act.
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## **5. OVERVIEW OF THE BUDGET**

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### **5.1 Balanced and Credible Budget**

The following National Treasury guidelines have been taken into consideration when preparing the budget:

- Tabling a balance and credible budget that is based on realistic estimates of revenue to be collected, taking into account both actual revenue collected in the past financial year, and revenue projects for the current financial year.
- The inclusion of all grants in the annual budget, on both the revenue and expenditure side;
- The presentation of three-year capital and operating budgets;
- The revision of the IDP to be consistent with the three-year budget;
- The maximum expenditure growth limit of 6.1% to stay within inflation targets as determined by National Treasury. The growth limit applies to own revenue sources only and excludes intergovernmental grants, for both the capital and operating budgets.
- Increases in rates and taxes have been kept within inflation targets, in support of government's macro-economic objectives and investor confidence.

### **Funding the Budget**

Section 18(1) of the MFMA states that an annual budget may only be funded from:

- Realistically anticipated revenues to be collected;
  - Cash backed accumulated funds from previous year's surpluses not committed for other purposes; and
  - Borrowed funds, but only for the capital budget
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Achievement of these requirements in totality effectively means that council has “balanced” its budget by ensuring that budgeted outflows will be offset by a combination of planned inflows.

### **Credible Budget**

Amongst other things, the following has been taken into consideration to ensure that this is a credible budget;

- Only activities consistent with the revised IDP have been included in the budget, taking into consideration the financial constraints of the municipality;
- It is achievable in terms of the agreed services delivery and budget implementation plan and performance targets;
- Contains revenue and expenditure projection that are consistent with current and past performance
- Does not jeopardize the financial viability of the municipality (ensures that the financial position is maintained within generally accepted prudential limits and that obligations can be met in the short, medium and long term; and
- Provided managers with appropriate levels of delegation sufficient to meet their financial management responsibilities.

The budget sets out certain service delivery levels and associated financial implications, therefore the community should realistically expect to receive these promised service delivery levels and understanding the associated financial implications.

## **5.2 Government Priorities Considered**

### **THE MTREF**

The budget has been prepared based on the new requirements and significant progress has been made on the implementation thereof. However, some processes

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are still being developed to ensure full compliance, which include activity based costing, asset management, system shortcomings, human capacity building amongst others.

Although the fact that our municipality is categorized as Low Capacity Municipality, it is also of outmost importance to ensure that Council complies with all legislative requirements, this entails the channelling of fund which would ordinarily be utilized for services delivery to the implementation of the legislative requirements.

In President Jacob Zuma's State of the Nation Address of 2017, he indicates government key priorities to be:

- Resolving the energy challenge
- Revitalising agriculture- Agri-Parks Programme, aimed at increasing the participation of small holder farmers in agricultural activities
- Creation of Job Opportunities
- Infrastructure investments
- Encouraging private investments
- Unlocking the potential of SMME's, cooperatives, townships and rural enterprise;
- Moderating work conflict

Therefore, in framing this budget, priority has been given to objectives and priorities of government based on the IDP to be adopted by council.

A bulk electricity purchase has increased drastically over the past two years as result of NERSA and ESKOM tariff increases. Bulk electricity price increase for 2017/18 from ESKOM will be 8% while municipalities budgeted for an increase of 10%, as this depends upon final approval by NERSA.

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The municipality has set aside R5 000 000 for electrification of rural areas in an attempt to reduce the backlog on access to electricity of communities.

The municipality has also embarked on reduction of electricity losses so as to attain almost full recovery of electricity costs, which in turn will result in timeous payments of the electricity provider.

In an attempt to addressing challenges faced by the underprivileged, as well as the successful implementation of the indigent campaign, the provision of free basic services and indigent subsidy are increasing in our new budget in comparison to previous years. Electricity income however is also increasing due to the higher demand based on more households having access to electricity, expansion of the municipality and the increase in municipal tariff.

The municipality is working towards the achievement of realising a surplus in future. The municipality will enter into a new agreement with Eskom for the recurring debt that was not catered for in the adjustment budget as soon it honours the current payment arrangement. Hence, there is an amount of R 50 000 000, that is set aside for Bulk purchase which includes the portion for the monthly usage.

The area of focus in the coming financial year will be mainly in collecting revenue, which is mainly on rates revenue and service charges, to ensure the financial viability of the municipality since there is an indication that Raymond Mhlaba Municipality is very much grant dependant at this stage. We are also embarking on reducing/management of Electricity losses due to illegal bridging and tempering in our areas.

The effective management of assets will also be a focus area to ensure that all assets are maintained and repair based on their conditions taking into account the cost effectiveness thereof. The Municipality is in a process of assessing the current fleet assets to ensure that all those assets that are no longer having economic value are disposed to avoid spending much on repairs and maintenance.

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More budget related policies/strategies will be developed to assist the municipality to control its revenue and expenditure in future. Changes were made to the existing budget related policies.

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## **6. EXECUTIVE SUMMARY**

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### **INTRODUCTION**

With the compilation of the 2017/18 Medium-Term Revenue and Expenditure Framework (MTREF), each department had to review its business planning processes taking into account their IDP objectives and individual departmental strategies. Business planning links back to priority needs and master planning, and essentially inform the detail operating budget appropriations and three-year capital programme. National Treasury's MFMA Circular No. 86 and 87 was mainly used to guide the compilation of the 2017/18 MTREF.

The 2016 Medium Term Budget Policy Statement emphasised that the global recovery from the 2008 financial crisis remains precarious, with growth forecast at 3.1 per cent in 2016 and 3.4 per cent in 2017. Domestic GDP growth for 2016 was forecasted at 0.9 per cent at the time of the 2016 Budget and it has since been revised to 0.5 per cent. It is anticipated that factors such as a more reliable electricity supply, improved labour relations, low inflation, a recovery in business and consumer confidence, stabilising commodity prices and stronger global growth will increase growth to 2.2 per cent by 2019. Furthermore, the country has experienced a decline in mining growth and weakened agricultural outputs as a result of the drought while growth in transport and telecommunications, electricity, gas and water have declined because of weakened demand. A conservative approach was thus followed for projecting revenue. Electricity supply constraints continues to limit growth and daunt investment. Exchange rate depreciation is contributing to a higher inflation outlook during 2016. These circumstances make it essential for municipalities to reprioritise expenditure and implement strict cost-containment measures.

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The compilation of the MTREF therefore remains a huge challenge to balance the budget between the limited revenue resources available and the immense need to provide quality service delivery to our community. Tariff increases must be limited to be within the affordability levels of our community and must still promote economic growth to ensure financial sustainability.

The municipality is not in a healthy financial position, however, it needs to at least stabilise and further strive to continuously better its financial position, coupled with acceptable levels of service delivery at affordable tariffs. The retention of sufficient cash-backed reserves is critical for the long-term sustainability of the municipality, and to this end the municipality is unable to achieve this objective. The municipality will try to build its cash-backed reserves by ensuring that all non-cash items are budgeted for and are cash-backed. This will be achieved by ensuring that the municipality stick to its plan and also embark on projects that are revenue generation in nature.

**Table 1 Consolidated Overview of the 2017/18 MTREF (R'000)**

| Description                           | Budget Year<br>2016/17 | Budget Year<br>2017/18 | Budget Year<br>2018/19 | Budget Year<br>2019/20 |
|---------------------------------------|------------------------|------------------------|------------------------|------------------------|
|                                       | Adjusted<br>Budget     |                        |                        |                        |
| <b>R thousands</b>                    |                        |                        |                        |                        |
| Total Revenue                         | 343 527                | 359 403                | 285 792                | 281 407                |
| Total Expenditure                     | 375 483                | 359 403                | 378 819                | 408 817                |
| Total Surplus /(Deficit)              | <b>(31 956)</b>        | <b>0</b>               | <b>(93 027)</b>        | <b>(127 410)</b>       |
| Total Capital Revenue Recognised      | 39 971                 | 47 633                 | 39 937                 | 42 105                 |
| Total Surplus/ (Deficit) for the year | <b>8 015</b>           | <b>47 633</b>          | <b>(53 090)</b>        | <b>(85 305)</b>        |

### **OPERATING REVENUE AND EXPENDITURE BUDGET**

The municipality's total budget amounts to R 407 036 355. Total operating revenue amounts to R359 403 205 and Capital transfers of R47 633 150. Total operating revenue has increased by 4,62 per cent or 15,876 million for the 2017/18 financial year when compared to the 2016/17 Adjustments Budget. For the two outer years, operational revenue decreased by 20.48 and 21.70 per cent respectively.



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The decrease is mainly due on the conditional grants to be received, such as demarcation grant, MIG capital grant and EPWP grant.

Total operating expenditure budget amounts to R 359 403 205 and translates into a balanced budget before capital transfers. When compared to the 2016/17 Adjustments Budget, operational expenditure has decreased by 4,28 per cent in the 2017/18 budget. The operating surplus, before capital grant transfers, for the two outer years decreases to a deficit of R93,027 million for the 2018/2019 financial year and R127,410 deficit in 2019/2020 as a result of the increasing operating expenditure, mainly due to non-cash items such as Debt impairment and Depreciation.

The municipality remains committed to a large capital programme with a significant portion funded by grants from National Government.

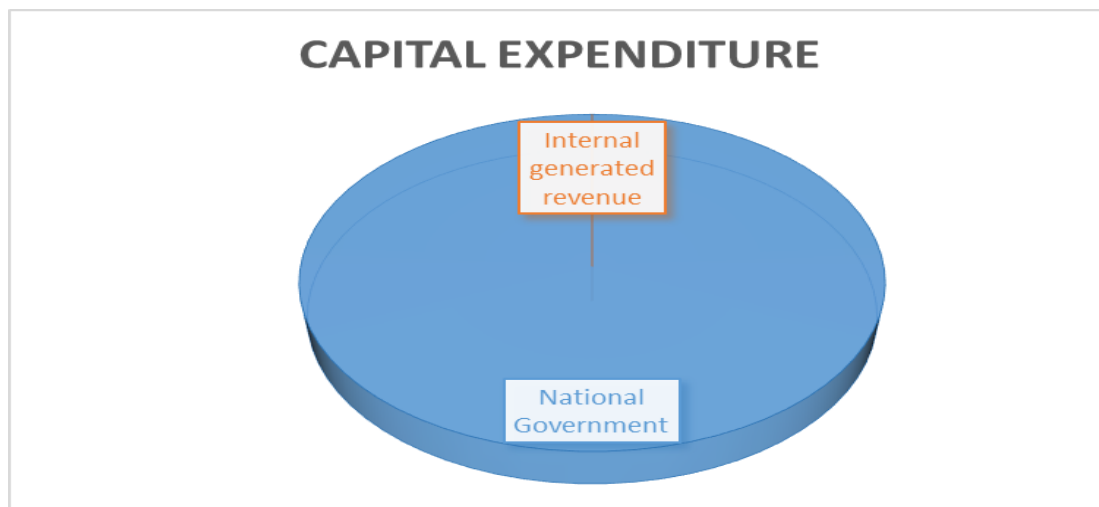
**Table 2 Total Capital Funding of the 2016/17 MTREF (R'000)**

| Description                           | Budget Year<br>2016/17 | Budget Year<br>2017/18 | Budget Year<br>2018/19 | Budget Year<br>2019/20 |
|---------------------------------------|------------------------|------------------------|------------------------|------------------------|
|                                       | Adjusted<br>Budget     |                        |                        |                        |
| <b>R thousands</b>                    |                        |                        |                        |                        |
| <b><u>Funded by</u></b>               |                        |                        |                        |                        |
| National Government                   | 38 471                 | 47 633                 | 39 937                 | 42 105                 |
| Transfers recognised- Capital         | <b>38 471</b>          | <b>47 633</b>          | <b>39 937</b>          | <b>42 105</b>          |
| Internal generated revenue            | 9 527                  | –                      | –                      | –                      |
| Total Surplus/ (Deficit) for the year | <b>47 998</b>          | <b>47 633</b>          | <b>39 937</b>          | <b>42 105</b>          |

The capital budget of R47,633 million for 2017/18 is 0,76 per cent less when compared to the 2016/17 Adjustment Budget. The capital programme decreases to R39,937 million in 2018/19 and R42,105 million in 2019/20. The decrease can mainly be attributed to the decrease in proposed expenditure to be financed from internally generated funds and a decrease in capital transfers – a trend that is set to continue throughout the MTREF.

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The municipality did not allocate a portion of the capital budget to be funded from own revenue due to the fact that the municipality does not have cash-backed reserves to fund its capital. The provision can be made in consultation with other departments to reduce their expenditures and be encourage where necessary to outsource funding to implement other project.



As indicated above no borrowing for capital projects is planned. The municipality is still well within the limits of its borrowing capacity, but will raise very limited leases in the near future in order to curtail possible rising debt servicing costs.

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### **7. Key Budget assumptions**

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#### **External factors**

Domestically, after five years of strong growth, during which about two million jobs were created, our economy shrank fast and millions of people lost their jobs. It is expected that recovery from this deterioration will be slow and uneven and that growth for 2017 will be minimal with a slightly better growth in the outer years.

Owing to the economic slowdown, financial resources are limited due to reduced payment levels by consumers. This has resulted in declining cash inflows, which has necessitated restrained expenditure to ensure that cash outflows remain within the affordability parameters of the Municipality's finances.

#### **General inflation outlook and its impact on the municipal activities**

There are five key factors that have been taken into consideration in the compilation of the 2017/18 MTREF:

- National Government macro-economic targets;
- The general inflationary outlook and the impact on Municipality's residents and businesses;
- The impact of municipal cost drivers;
- The increase in prices for bulk electricity; and
- The increase in the cost of remuneration.

#### **Collection rate for revenue services**

The base assumption is that tariff and rating increases will increase at a rate of CPI over the long term. It is also assumed that current economic conditions, and relatively controlled inflationary conditions, will continue for the forecasted term.

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The rate of revenue collection is currently expressed as a percentage of annual billings. The collections of the municipality on outstanding debtors are anticipated to increase during the coming financial period due to implementation of effective credit control and the revenue enhancement strategy and financial recovery plan to be developed. It should however be noted that the revenue budgeted for are 100% based on billing and therefore we need to explore and implement effective controls to increase our billing capacity to decrease our current grant dependency. Hence the municipality is anticipating to collect the actual revenue of R 128 915 980.

### **Growth or decline in tax base of the municipality**

Debtors' revenue is assumed to increase at a rate that is influenced by the consumer debtors' collection rate, tariff/rate pricing, real growth rate of the municipality, household formation growth rate and the poor household change rate.

### **Draft Tariff increases**

It should be noted that the tariffs are attached as an annexure to the budget due to the complexity of the tariffs versus the budget schedule.

- Service charges – Electricity tariffs will increase by 10% for 2017/2018 financial subject to NERSA approval. This is based on the average cost of rendering the service.
  - Property rates tariffs – there will be no changes on the property rates tariffs for the former Nkonkobe municipality. However, there will be three additional categories under residential category. Decision was taken that former Nxuba tariffs on property rates must match the ones for former Nkonkobe over the next three years. Therefore, an increase of 25% on property rates tariffs will be imposed. It should also be noted that for business category, the tariff will increase by 100% to match the tariff for former Nkonkobe municipality.
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- General (Other Tariffs) – Former Nkonkobe tariffs will increase by the CPI rate of 6% and for former Nxuba, tariffs (Phase in) by 50% in order to make them cost related.
- Interest on investments – We aim to put more monies on our short term investment accounts resulting in an increase of interest received.
- Interest on outstanding debtors – Based on the more effective implementation of the credit control and debt management policy it is expected to decrease.

### **Salary increases and Council Remuneration**

There is a collective agreement on salary increases in place for the budget year. Based on the circular and the notch increase we have budgeted for 6% plus 1% per cent increase for the 2017/2018 period and 7% for senior managers.

The budget for the council remuneration has been increased by 6% compared for 2017/2018 financial year.

### **Impact of national, provincial and local policies**

Integration of service delivery between national, provincial and local government is critical to ensure focussed service delivery and in this regard various measures were implemented to align IDPs, provincial and national strategies around priority spatial interventions. In this regard, the following national priorities form the basis of all integration initiatives:

- Creating jobs;
  - Enhancing education and skill development;
  - Improving Health services;
  - Rural development and agriculture; and
  - Poverty Alleviation
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To achieve these priorities integration mechanisms are in place to ensure integrated planning and execution of various development programs. The focus will be to strengthen the link between policy priorities and expenditure thereby ensuring the achievement of the national, provincial and local objectives.

### **Ability of the municipality to spend and deliver on the programmes**

It is estimated that a spending rate of 100% will be achieved over the MTREF period.

Budgets are prepared in an environment of uncertainty. To prepare a meaningful budget, assumptions are made about internal and external factors that could influence the Annual Budget.

### **Other assumptions:**

- **Investments**

Raymond Mhlaba municipality does not have long-term investments, only call accounts which are included in the cash and cash equivalents as per our annual financial statements.

- **Borrowing**

The municipality is not in a process of applying for any loans.

### **Service delivery**

As part of the improvement of service delivery, more strategies will need to be developed and implemented to ensure that we meet the needs of the community and eliminates factors that have a negative effect on councillors' finances.

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### **Implementation of GRAP**

The municipality will fully implement GRAP in 2016/2017 financial year, since it is a new entity. FMG (grant received from National Treasury) and own revenue is used to maintain compliance with GRAP. In the 2017/2018 budget, a budget has been set aside to assist with implementation of mSCOA and GRAP to ensure that the municipality complies.

The project also involves the review of the current Asset Management Policy to be aligned to GRAP standards and other policies.

### **Internal Charges**

The current method of cost recovery between service departments must be reviewed in terms of Activity Based Costing Principles and Standards. Activity based costing principles if correctly applied, will ensure that all costs applicable to a specific service are recorded. This means that tariff setting will be improved. Our current financial system cannot perform this function and due to capacity problems within the finance department, this function will be done by the affected departments.

### **Functions outsourced and functions performed on agency basis**

- No municipal services have been contracted out to section 21 or Proprietary Limited companies other than there one for external securities.  
Agent for Department of Roads and Transport on certain e-Natis transactions.

### **Operating Budget**

The 2017/2018 operating expenditure budget amounts to R359,403 million (including non-cash items).

### **Capital Budget**

The 2017/2018 capital budget amounts to R47,633,000 million. (Including MIG).

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### **Employee cost and other expenditure to total Operating expenditure**

The total employee cost for 2017/2018 including Councillor Allowance amounts to 53% of the total operating expenditure (Excluding non-cash items). It should be noted that the casual wages, standby allowances and overtime are included as part of employee related cost. Furthermore, the increase in employee related costs does not cater for the salaries that are being funded by grants.

Total operating expenditure amounts to R359,403 million in 2017/18. The municipality has set aside an amount of R 5,170 million, R 2 million being funded from MIG and R3,170 million. It should furthermore be noted that the Transfers and grants are R 19, 200 million of the total operating expenditure, and are based on the free basic services to indigents in our community and grants paid to Raymond Mhlaba agency.

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